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No. 02 1552 MAR 12 2003

OFFICE OF THE CLERK

In The

Supreme Court of the United States

PALAIS ROYAL, INC and 3 BEALL BROTHERS 3, INC.,

Petitioners,

v.

CAROLE KEETON STRAYHORN, COMPTROLLER OF PUBLIC ACCOUNTS OF THE STATE OF TEXAS, et al.,

Respondents.

On Petition For Writ Of Certiorari To The Third Court Of Appeals Of Texas, Austin

PETITION FOR WRIT OF CERTIORARI

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49 pp

QUESTIONS PRESENTED

Did the implementation of the Texas earned surplus tax violate the constitutional requirements of equal protection and due process by taxing Petitioners and other fiscal year taxpayers on income earned in 1990, when calendar year taxpayers were not taxed on such income?

Did the implementation of the Texas earned surplus tax violate due process and the takings clause by taxing income earned nineteen months before the enactment date?

PARTIES

Petitioners

Palais Royal, Inc. and 3 Beall Brothers 3, Inc.
Petitioner Beall Brothers merged with Petitioner Palais Royal on August 2, 1993. Petitioner Palais Royal is wholly owned by Stage Stores, Inc., a publicly held company.

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OPINIONS BELOW

The decisions of the Texas Supreme Court denying the petition for review and Petitioner's motion for rehearing (Appendix 17) are not reported. The opinion of the Court of Appeals (Appendix 1) is reported at 81 S.W.3d 909 (Tex. App. – Austin 2002). The judgment of the trial court is not reported (Appendix 14).

JURISDICTION

On December 19, 2002, the Texas Supreme Court denied Petitioner's motion for rehearing of the denial of the petition for review. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1257.

CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS INVOLVED

U.S. CONST. amend. XIV, § 1:

> Section 1. Citizens of the United States.
>
> All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

U.S. CONST. amend. V:

> No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

STATEMENT OF THE CASE

On August 22, 1991, the Texas Legislature imposed a franchise tax on earned surplus, which was codified in Texas Tax Code section 171.002. Appendix 20. In the same act, the Legislature added Texas Tax Code section 171.110, which based earned surplus on a corporation's adjusted federal taxable income. Appendix 21. Prior to that time, the State of Texas had no corporate income tax or any tax measured by income. The State began taxing Petitioners' income earned beginning in February 1990 while taxing other corporations' income earned beginning in January 1991, based solely on the taxpayers' accounting years. The Petitioners filed a motion for summary judgment arguing that this discrimination was unconstitutional because it lacked a rational basis. The trial court granted Petitioners' motion on this ground. Appendix 14. The Austin Court of Appeals reversed this decision. Appendix 1. The Texas

Supreme Court then denied the petition for review and Petitioner's motion for rehearing. Appendix 17.

REASONS FOR GRANTING THE WRIT

The Texas earned surplus tax was implemented in 1992 and applied to Petitioners' income earned almost two years earlier.

The Texas franchise tax is an annual tax on the privilege of doing business in the State. Tex. Tax Code § 171.001 (Vernon 2002). However, instead of basing the annual tax on the business done during the privilege year, the Legislature based the tax on an earlier year's business. Specifically, the tax for a calendar year "privilege period" is based on the corporation's accounting period that ended in the previous year. *Id.* § 171.1532(b) (Appendix 23). In addition to the annual earned surplus tax, corporations are also required to pay an "additional" earned surplus tax when they cease doing business in the State. *Id.* § 171.0011 (Appendix 19). The "additional" earned surplus tax begins on the date that the regular franchise tax ends, and ends on the last day that the corporation does business in the State.

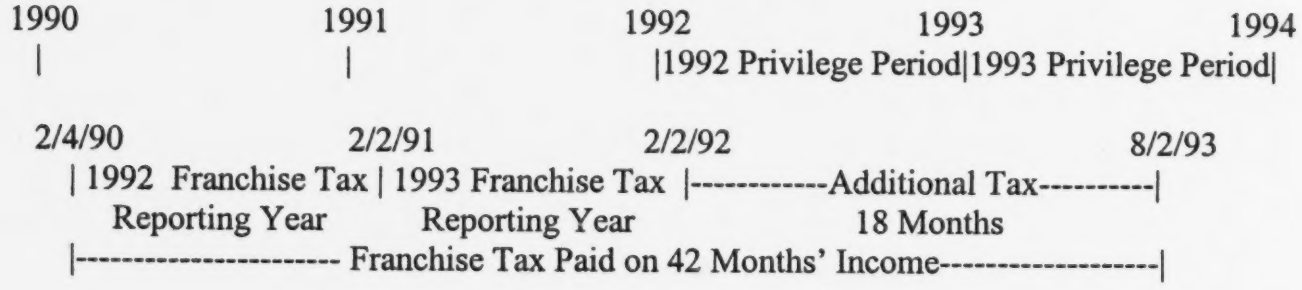
The Petitioners used a "52-53 week" accounting period ending on the Saturday nearest to January 31. Thus, for the privilege of doing business in Texas for calendar year 1992, the Texas franchise tax statute required the Petitioners to base their 1992 franchise tax on the income earned in their accounting year beginning February 4, 1990 and ending February 2, 1991. Because of the difference between the privilege periods and the reporting periods, the Petitioners' tax returns were based on income

earned almost two years earlier. Also, after Petitioner Beall Brothers merged with Petitioner Palais Royal on August 2, 1993 and ceased doing business in the State, it was required to pay the "additional" earned surplus tax for eighteen additional months.

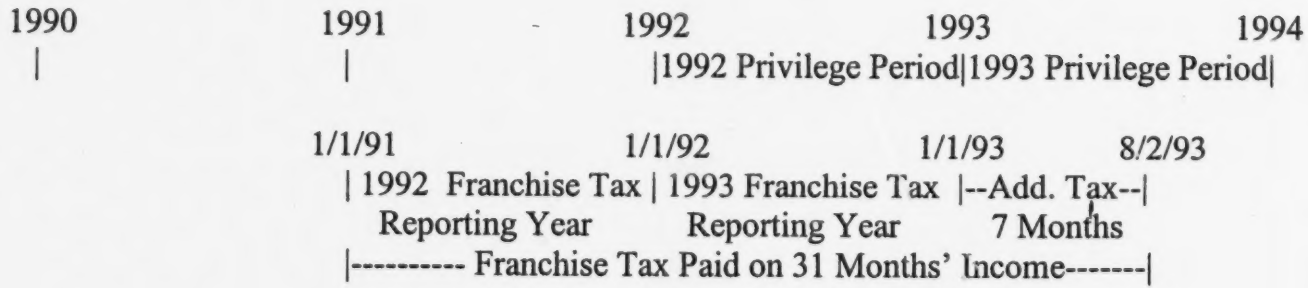
The implementation of the Texas earned surplus tax discriminated against Petitioners.

The discrimination is illustrated by the following time lines comparing Petitioner Beall Brothers with a calendar year-end taxpayer, each of whom did business in Texas during 1992 and 1993, paid tax on earned surplus for the privilege of doing business in 1992 and 1993, and ceased doing business in Texas on August 2, 1993:

3 Beall Brothers 3 (Fiscal Year-End Taxpayer)



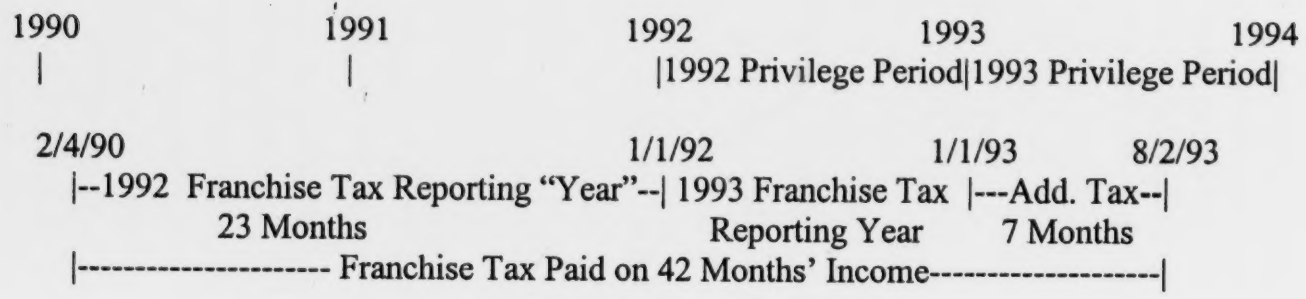
Calendar Year-End Taxpayer



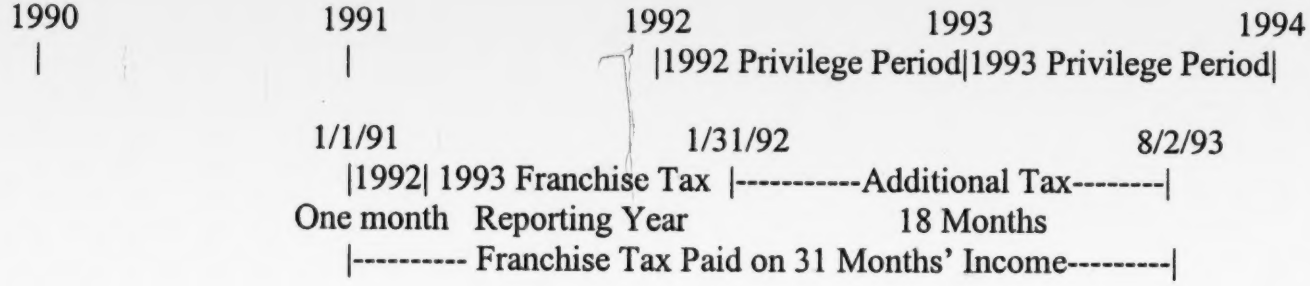
The time lines show that Petitioners and other fiscal year-end taxpayers were taxed on income earned in 1990, while calendar year-end taxpayers will never be taxed on 1990 income. In addition, because of the different starting dates for the earned surplus tax, Petitioners and other fiscal year-end taxpayers will ultimately pay more franchise taxes on income earned over longer periods than calendar year-end taxpayers for the same privilege of doing business. Court Record ("**CR**") 367 (Comptroller expert deposition at 10). This discrimination was systematic and pervasive. There were 31,563 fiscal year-end taxpayers who paid franchise taxes on 1990 income compared to 57,516 calendar year-end taxpayers who did not pay franchise taxes on 1990 income. CR 340-341 (Answer to Interrogatory 3, Defendants' Response to Plaintiffs' Second Interrogatories).

Petitioners could not have avoided the discrimination by changing their accounting year-ends to December 31. As the following time line shows, Beall Brothers would have paid the earned surplus tax for the same period of time and would have been in a worse position because it would have accelerated the tax due, paying tax on 23 months' income for its first report. By contrast, a calendar year-end taxpayer could change to a January 31 fiscal year-end, and improve its position by paying tax on only one month's income for the privilege of doing business for the first year (or any other year). This discrimination exists solely because of Petitioners' fiscal accounting year-ends:

If 3 Beall Brothers 3 Changed to Calendar Year-End Taxpayer



If Calendar Year-End Taxpayer Changed to January 31 Fiscal Year-End



The implementation of the earned surplus tax violated the constitutional requirements of equal protection and due process by taxing Petitioners and other fiscal year taxpayers on income earned in 1990, when calendar year taxpayers were not taxed on such income.

The implementation of the franchise tax was unconstitutional because similarly situated taxpayers were treated differently based solely on their accounting year-ends. Petitioners and other fiscal year-end taxpayers were required to pay more earned surplus taxes than calendar year-end taxpayers for exactly the same privilege of doing business, and the State cannot rationally justify this discrimination.

There is no justification for the discrimination based on conformance to federal tax periods and administrative convenience.

The "legitimate" goals advanced by the Court of Appeals are "convenience, reliability, and efficiency, and conformity to federal tax periods." Appendix 7. The opinion does not explain how the legislation achieves these goals; and, in fact, the legislation does not achieve these goals.

With regard to "conformity to federal tax periods," it is important to note that Petitioners are not challenging the use of accounting and federal tax periods as franchise tax base periods. Petitioners are only challenging the disparity in the implementation date of the tax, which Petitioners contend should be the same for all taxpayers. The unequal taxation results not from the use of accounting years as reporting periods, but from the use of accounting year-ends to start the tax at different times for different taxpayers. If the State had started the earned surplus tax at

the same time for all taxpayers, there would be no equal and uniform taxation claim.

There is no convenience, reliability, or efficiency associated with using accounting year-ends to implement the tax at different times for different taxpayers, as compared with implementing the tax at the same time for all taxpayers. In the Petitioners' case, as is the case with many taxpayers, financial records are kept on a monthly basis. The Petitioners easily, and without objection from the State, identified their earned surplus earned on and after January 1, 1991 in order to be treated the same as calendar year-end taxpayers. *See* CR 352-357 (Affidavit of Stephen N. Cook and supporting exhibits). If, for some reason, a taxpayer did not keep monthly records, the tax could be prorated based on annual data.

Ironically, except for the initial earned surplus tax returns of existing taxpayers such as Petitioners, who were already doing business in Texas when the earned surplus tax was implemented, the State does not use accounting year-ends to start the initial earned surplus tax for new taxpayers. When a new taxpayer first starts doing business in the State, the tax starts on the date the taxpayer begins business in the State, which may be in the middle of the taxpayer's accounting year. Tex. Tax Code § 171.1532(a) (Appendix 23). The Texas franchise tax rate is then prorated on the initial return.[1] The State could

[1] *See* Tex. Tax Code section 171.1532(a) (Appendix 23). *See also*, Comptroller Form 05-364 "INSTRUCTIONS FOR COMPLETING FRANCHISE TAX REPORTS ORIGINALLY DUE ON OR AFTER JANUARY 1, 1992," which states: "NOTE: Because the privilege period for the initial report covers more than one year, the tax rate for the

(Continued on following page)

have easily adopted a similar system for existing taxpayers when the tax was implemented in 1992, without any additional record-keeping or reporting requirements. Therefore, the State cannot use administrative convenience to justify the taxation of fiscal year-end taxpayers such as Appellants for eleven additional months of income.

Even under a rational basis threshold, the equal protection analysis requires a comparison of the efficiency achieved with the degree of discrimination that is purported to be justified. For example, suppose the State adopted a franchise tax calculated by multiplying the number of letters in the corporate name by a tax rate. Like a classification based on accounting year-ends, a classification based on letters in a corporate name has no rational relationship to the amount of business done in the State by a corporation or to the privilege of doing business in the State.[2] However, under the State's simplistic analysis, a franchise tax based on the number of letters in the corporate name would be constitutional because it would be indisputably easier and more efficient to administer than

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taxable capital calculation on Schedule A and the additional tax calculation on Schedule B [earned surplus] will be greater than the annual rate." http://www.window.state.tx.us/taxinfo/taxforms/05-364.pdf. *See also*, Comptroller Form 96-114, which states: "A preprinted report with a *prorated* tax rate will be mailed to the corporation about two months before the report is due." http://www.window.state.tx.us/taxinfo/taxpubs/tx96_114.html (emphasis added).

[2] Q: Would you agree with me that a taxpayer's fiscal year is not related to the amount of business that a taxpayer does in the State?

A: Yes.

CR 408 (Comptroller expert deposition at 51).

a franchise tax based on the complicated reporting required for a franchise tax based on taxable capital or earned surplus. Petitioners submit that no simplistic assertion of administrative efficiency can justify the imposition of eleven months more tax on a fiscal year-end taxpayer when no administrative efficiency is established and there is no rational relationship between a corporation's fiscal year and the amount of business it does in the State.

The administrative convenience issue in this case is similar to the issue in *Rinaldi v. Yeager*, in which the State of New Jersey seized the prison earnings of the Plaintiff to pay for the cost of his trial transcript while it did not impose a similar burden on convicted persons who were not serving sentences in prison. *Rinaldi v. Yeager*, 384 U.S. 305 (1966). The State of New Jersey asserted that the discrimination was justified because it was administratively convenient to collect the fees from prison inmates. The United States Supreme Court rejected this argument:

> Finally, the classification established by the statute cannot be justified on the ground of administrative convenience. Any supposed administrative inconvenience would be minimal, since repayment could easily be made a condition of probation or parole, and those punished only by fines could be reached through the ordinary processes of garnishment in the event of default.

Id. at 310. In this case, any supposed administrative convenience would also be minimal, since the tax-reporting period could have been started in the middle of a taxpayer's accounting year, just as it is currently started in the middle of an initial taxpayer's accounting year. There is simply no rational basis for constructing a tax

system that imposes eleven extra months of tax on some taxpayers solely because of their accounting year, when there was an equally practical system that would have treated all taxpayers equally. *See also, Williams v. Vermont*, 472 U.S. 14, 23 n. 8 (1985) ("But the choice of a proxy criterion . . . cannot be so casual as this when a more precise and direct classification is easily drawn."); *Kraft General Foods v. Iowa Department of Revenue*, 505 U.S. 71, 81 (1992) ("administrative convenience" rejected when there were "reasonable nondiscriminatory alternatives"). Because there was no rational basis for the discrimination, the discrimination was unconstitutional.

There was discrimination.

The Court of Appeals opinion implies that there was no discrimination because "the earned-surplus amendments have a uniform starting date, tax base, and tax rates." Appendix 7. However, the earned surplus tax did not have a uniform starting date. The annual privilege periods for all taxpayers may have started on January 1, 1992, but the reporting periods varied based on the taxpayers' accounting year-ends. Petitioners paid earned surplus taxes on income earned in 1990, while calendar year-end taxpayers escaped all earned surplus taxation on their 1990 incomes.

The Court of Appeals opinion also states: "All taxpayers were required to pay taxes based on a twelve-month period ending on or before December 31, 1991." Appendix 7. This statement is also incorrect because, as previously explained, calendar year-end taxpayers could change to fiscal year-end taxpayers and pay tax on less than one

year's income. Petitioners did not have a similar opportunity.

The 1992 franchise tax year, taken in isolation, may not appear to be discriminatory because fiscal year-end taxpayers and calendar year-end taxpayers who did not change their accounting years all paid tax on twelve months' income for the privilege of doing business for one year. However, the regular earned surplus imposed by Texas Tax Code section 171.001 cannot be viewed in isolation from the "additional" earned surplus tax imposed by Texas Tax Code section 171.0011 (Appendix 19). The different starting dates for implementing the earned surplus tax, combined with the different periods of "additional" earned surplus tax, resulted in Appellants paying more tax over a longer period than an identical company with a calendar year-end, for exactly the same privilege of doing business in the State.

The "additional" earned surplus tax was adopted by the same legislation, is computed in exactly the same manner as the regular earned surplus tax, and starts immediately after the regular earned surplus tax ends. The "additional" earned surplus tax and the regular earned surplus tax must be viewed together because the regular earned surplus tax was used by the Texas courts to uphold the validity of the "additional" earned surplus tax in *Rylander v. 3 Beall Brothers 3, Inc.*, 2 S.W.3d 562 (Tex. App. – Austin 1999, pet. denied).

Considered in isolation, the "additional" earned surplus tax is unconstitutional because there is no rational basis for imposing an income tax on Beall Brothers for eighteen months while imposing a seven-month tax on a calendar year-end taxpayer that left the state on the same

day. However, the State contended that "the additional tax is designed to reduce tax revenue losses [to the regular earned surplus tax] caused by corporation reorganizations." *Id.* at 565. Specifically, the State contended, as it contended by affidavit in this proceeding, that without the "additional" earned surplus tax, corporations could engage in annual mergers with shell corporations and avoid paying the regular earned surplus tax. The Court of Appeals accepted this argument and concluded that the "additional" tax was constitutional because of its relationship to the regular earned surplus tax:

> In each scenario, the beginning date of the additional tax period represents the first day on which the regular franchise tax was no longer applicable. Moreover, the ending date represents the first day Bealls was no longer subject to the taxing jurisdiction of this state in relation to the tax on net taxable earned surplus. Therefore, the additional tax applies even-handedly because the amount of the tax is always based upon the period of previously untaxed earned surplus.

Id. at 570. The Court accepted the State's contention and justified the "additional" earned surplus tax as necessary to close a loophole in the regular earned surplus tax. Therefore, the State cannot now assert that the regular earned surplus tax is unrelated to the "additional" earned surplus tax and may be considered in isolation. As the Court of Appeals did in the *Beall Brothers* case, this Court must evaluate the entire tax structure, and not just a piece of it.

When the State included the "additional" earned surplus in the tax scheme, it abandoned the accounting

year standard because the tax period for the "additional" earned surplus tax is not based on an annual accounting period. Having abandoned the accounting year standard on the back end of the tax and imposed a system that terminated the tax at the same time for all taxpayers who left the state at the same time, the State cannot now claim that the accounting year standard is essential on the front end of the tax and start the tax at different times for different taxpayers, such that the earned surplus tax is imposed for different lengths of time for similarly situated taxpayers. This is unconstitutional discrimination without a rational basis.

The implementation of the earned surplus tax violated due process and the takings clause by taxing income earned nineteen months before the enactment date.

As previously stated, the Legislature adopted the earned surplus tax in August 1991 and applied it retroactively to Plaintiffs' income earned beginning in February 1990. At the time of its adoption, the earned surplus tax was not merely a change to an existing tax – it was an entirely new measure of taxation based on income, where no such tax existed before. This act, applied retroactively to income earned nineteen months before its adoption, violated the due process clause and the just compensation clause of the United States Constitution.

In *Blodgett v. Holden,* this Court recognized that "a tax may be so arbitrary and capricious that its enforcement would amount to deprivation of property without due process of law within the inhibition of the Fifth Amendment." *Blodgett v. Holden,* 275 U.S. 142, 147 (1927). In the *Blodgett* case, Congress attempted to apply a

newly-adopted gift tax to a gift given before the statute was adopted. The Court held: "It seems wholly unreasonable that one who, in entire good faith and without the slightest premonition of such consequence, made absolute disposition of his property by gifts should thereafter be required to pay a charge for so doing." *Id.* Here too, it is wholly unreasonable for the Texas Legislature to have taxed income earned nineteen months before the adoption of legislation that, for the first time, taxed corporate income.

Also, in *Eastern Enterprises v. Apfel*, the United States Supreme Court recognized that retroactive economic legislation may result in an unconstitutional taking. *Eastern Enterprises v. Apfel,* 524 U.S. 498 (1998). The Court held that "the process for evaluating a regulation's constitutionality involves an examination of the 'justice and fairness' of the governmental action." *Id.* at 523. The inquiry "does not lend itself to any set formula" and "is essentially ad hoc and fact intensive." *Id.*

Although the State may impose retroactive legislation "confined to short and limited periods" (*id.* at 528), this is not such a case. The effect of the earned surplus tax legislation was not limited to the year in which it was enacted – it went back nineteen months prior to its enactment date of August 22, 1991 and taxed income earned as early as February 1990. Furthermore, the legislation interfered with the "reasonable investment backed expectations" (*id.* at 523) of the Petitioners. When Petitioners were earning the income at issue in 1990, they could not have anticipated that the Legislature would enact an entirely new measure of franchise taxation on income that had not previously existed. Furthermore, Petitioners were powerless to change their accounting years to minimize

their tax burden or prevent the discrimination. In fact, if Petitioners had changed their accounting years to have calendar year-ends, they would have accelerated their tax payment because the first earned surplus period would have covered a 23-month period instead of a 12-month period.[3]

In this case, the economic impact of the legislation was substantial and unfair. It exposed fiscal year-end taxpayers such as Petitioners to taxation for up to eleven months of additional income earned in 1990, while calendar year-end taxpayers escaped taxation of this income. This discrimination was based solely on the fiscal year-ends of the taxpayers. The State had no legitimate reason to exact this severe punishment on Petitioners and other fiscal year-end taxpayers. The Court should conclude that this legislation is a violation of due process and an unconstitutional taking.

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[3] Q: The bottom line is that if 3 Beall Brothers had switched its accounting year to a calendar year, it would still have had to pay earned surplus tax for a 42-month period, correct?

A: Yes.

Q: And, in fact, it would have been worse off than it actually was, because the earned surplus tax would be accelerated in the sense that its first return would cover a 23-month period instead of a 12-month period?

A: If by "worse off," you mean they would have to pay it sooner, in 3 Beall Brothers, probably so . . . .

CR 402 (Comptroller expert deposition at 45); *see* 34 Tex. Admin. Code § 3.544(a)(1)(C) (West 2002) (stating the beginning and ending dates for franchise tax-reporting periods).

CONCLUSION

For these reasons, Petitioners request the Court to grant this petition for writ of certiorari. It is irrational to impose significant additional taxes on fiscal year-end taxpayers when the taxpayers' accounting years have no relation to the value of doing business in the State. This Court should correct the Court of Appeals' opinion, which will otherwise create a dangerous precedent, enabling future legislatures to implement tax schemes that arbitrarily impose burdens on classes of taxpayers without a rational basis.

Respectfully submitted,

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81 S.W.3d 909

Court of Appeals of Texas,
Austin.

Carole Keeton RYLANDER, Successor-In-Interest to John Sharp, Comptroller of Public Accounts of the State of Texas; and John Cornyn, Successor-In-Interest to Dan Morales, Attorney General of the State of Texas,
Appellants,
v.
PALAIS ROYAL, INC. and 3 Beall Brothers 3, Inc.,
Appellees.

No. 03-01-00224-CV.

July 26, 2002.

Christine Monzingo, Assistant Attorney General, Austin, for Appellants.

Ray Langenberg, Mark W. Eidman, Scott, Douglas & McConnico, L.L.P., Austin, for Appellees.

Before Justices *KIDD*, YEAKEL and *PATTERSON*.

LEE YEAKEL, Justice.

Appellants Carole Keeton Rylander, Comptroller of Public Accounts of the State of Texas, and John Cornyn, Attorney General of the State of Texas,[1] appeal from a summary judgment in favor of appellees Palais Royal, Inc. and 3 Beall Brothers 3, Inc. (together "Bealls"), arising from a tax-protest suit. *See* Tex. Tax Code Ann. § 112.052

[1] The comptroller and attorney general are statutory defendants in tax-protest suits. *See* Tex. Tax Code Ann. § 112.151(b) (West 2001). Their interests do not diverge. We will therefore refer to them jointly as the "Comptroller."

(West 2001).[2] The district court found the implementation of the earned-surplus amendments to the franchise tax act unconstitutional and ordered the Comptroller to refund franchise taxes paid by Bealls. *See id.* § 171.002, .110, .152, .1532. The Comptroller appeals. We will reverse and render.

THE CONTROVERSY

This dispute arises out of Bealls' August 2, 1993 cessation of business in Texas for franchise-tax purposes due to its merger with Palais Royal, Inc. Following the merger, Bealls has continued to operate in Texas under the "Bealls" name but is owned and operated by Palais Royal. This Court has previously considered the application of the portion of the 1991 franchise tax act amendments providing for an "additional tax"[3] to the Bealls/Palais Royal merger. *See Rylander v. 3 Beall Brothers 3, Inc.*, 2 S.W.3d 562 (Tex.App.-Austin 1999, pet. denied) (*"Beall Brothers I"*). The 1991 amendments also added a corporation's earned surplus to the tax base from which to calculate the corporation's franchise-tax liability. *See* Act of Aug. 13, 1991, 72d Leg., 1st C.S., ch. 5, § 8.03, 1991 Tex. Gen. Laws 153, *amended by* Act of May 30, 1999, 76th Leg., R.S., ch. 394, § 10, 1999 Tex. Gen. Laws 2454, 2454-55

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[2] The parties rely on the 1992 code for this provision as it was the version in effect during the audit period at issue. The amendments to this provision do not materially affect our case; therefore, we cite to the current code for convenience.

[3] *See* Act of Aug. 13, 1991, 72d Leg., 1st C.S., ch. 5, § 8.02, 1991 Tex. Gen. Laws 152, *amended by* Act of May 27, 1993, 73d Leg., R.S., ch. 546, § 1, 1993 Tex. Gen. Laws 2043 (current version at Tex. Tax Code Ann. § 171.110 (West 2001)).

(current version at Tex. Tax Code Ann. § 171.002 (West 2001)). In *Beall Brothers I,* we described the Texas franchise-tax scheme appropriate to the circumstances of the current controversy, with citations to applicable authority. *See* 2 S.W.3d at 564-65. In the interest of brevity, we will generally describe here that scheme without citation.

The Texas franchise tax is imposed on the value of the privilege of doing business in Texas. The tax is imposed annually on each corporation that is incorporated in Texas or that conducts business in Texas. A corporation's franchise-tax liability is based on the business done by the corporation during its last accounting period ending in the year before the year in which the corporation's tax report is due (the "privilege period"). The tax is calculated by multiplying the franchise-tax base by the franchise-tax rate.

Before 1992, the franchise-tax base was comprised solely of a corporation's "taxable capital." Taxable capital included the corporation's "stated capital" and "surplus." Stated capital is the sum of the par value of all shares of the corporation having a par value that have been issued plus the consideration fixed by the corporation for all shares without par value that have been issued. Surplus is the corporation's net assets less its stated capital. Under this plan, capital-intensive industries bore the brunt of the tax, even in unprofitable years. In 1991 the legislature amended the franchise-tax act to establish "earned surplus" as the tax base from which to calculate the major portion of a corporation's franchise tax. Earned surplus is the corporation's reportable federal net income, less certain foreign-source income, plus officer and director compensation. As applicable here, "[t]he rates of the franchise tax are . . . 0.25 percent per year of privilege

period of net taxable capital; and . . . 4.5 percent of net taxable earned surplus." Tex. Tax Code Ann. § 171.002(a) (West 2001).

The amendments were effective January 1, 1992 and "appl[y] to reports originally due on or after that date." Act of Aug. 13, 1991, 72d Leg., 1st C.S., ch. 5, art. 8, § 8.27(a), 1991 Tex. Gen. Laws 134, 167. By its own election, Bealls operated as a fiscal-year taxpayer, as opposed to a calendar-year taxpayer, and utilized a fiscal year ending on the Saturday nearest January 31. Thus, the privilege period for the franchise-tax report required to be filed by Bealls in 1992 was the period from February 4, 1990 to February 2, 1991, the accounting period that ended in the year before the tax report was due. Because the earned surplus to be included in Bealls' 1992 report was based on federal taxable income earned in the fiscal or calendar year ending on or before December 31, 1991, Bealls' 1992 franchise tax was based on the income reported for the fiscal year ending February 2, 1991, the Saturday nearest January 31, 1991. This resulted in Bealls owing a franchise tax computed on income earned beginning in February 1990, in contrast to calendar-year taxpayers who owed the tax computed on income earned beginning in January 1991.

Simply put, because of its fiscal year, Bealls' first tax report following the 1991 amendments was due May 15, 1992, the report date in the year – 1992 – following the year in which Bealls' accounting period ended – February 2, 1991. Bealls is thus obligated to base its franchise tax due in 1992, in part, on income earned in 1990, since a portion of its fiscal year ending February 2, 1991 – February 4, 1990 through December 31, 1990 – precedes calendar year 1991. A calendar-year taxpayer is only obligated

to include 1991 income in its 1992 report because its accounting year ends December 31, 1991.

Bealls paid the tax under protest and filed suit for a refund.[4] *See* Tex. Tax Code Ann. § 112.052. Both parties filed motions for summary judgment. The district court granted Bealls' motion and denied the Comptroller's, finding that the earned-surplus amendments were unconstitutional as applied to Bealls, and ordered the Comptroller to refund a total of $480,383.80 in tax plus interest assessed on that amount by the Comptroller and statutory interest provided by the tax code. *See id.* § 112.060. Additionally, the district court found that Bealls was "entitled to a business-loss carryover of $4,345,079 for the Report Year 1992."[5] The Comptroller now appeals by three issues.

STANDARD OF REVIEW

The parties either stipulate to or do not dispute the material facts in this case. Therefore, whether the district

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[4] The amendments to the franchise tax also included an "additional tax," which is levied on a corporation that is subject to the franchise tax but is no longer subject to the taxing jurisdiction of the State in relation to the tax on net taxable earned surplus. *See* Tex. Tax Code Ann. § 171.110. These additional taxes were paid by Bealls when it merged with Palais Royal and ceased doing business in Texas. The tax-protest suit that arose from that tax was previously resolved by this Court and is not before us here. *See Rylander v. 3 Beall Bros. 3, Inc.*, 2 S.W.3d 562 (Tex.App.-Austin 1999, pet. denied); *see also Universal Frozen Foods v. Rylander*, 78 S.W.3d 588 (Tex.App.-Austin 2002, no pet. h.).

[5] The judgment also provided that "[w]ith regard to [Bealls'] constitutional claims concerning officer and director compensation, the Court grants [the Comptroller's] Motion for Summary Judgment and denies [Bealls'] Motion for Summary Judgment." Neither party has appealed this portion of the district-court judgment.

court properly granted summary judgment is a question of law, and we will review the district court's decision *de novo*. *See Natividad v. Alexsis, Inc.*, 875 S.W.2d 695, 699 (Tex.1994); *Nixon v. Mr. Prop. Mgmt. Co.*, 690 S.W.2d 546, 548-49 (Tex.1985). When the parties file competing motions for summary judgment and one is granted and the other denied, the reviewing court should review the summary-judgment evidence presented by both sides and determine all questions presented. *Commissioners Court v. Agan*, 940 S.W.2d 77, 81 (Tex.1997). The district court's final judgment states that Bealls' motion for summary judgment was granted on its "constitutional claims." However, Bealls raised several constitutional claims and the judgment does not specify which the district court found persuasive. Therefore, the Comptroller must attack each claim raised by Bealls in its motion for summary judgment. *See State Farm Fire & Cas. Co. v. S.S. & G.W.*, 858 S.W.2d 374, 381 (Tex.1993).

DISCUSSION

Equal Taxation and Equal Protection Claims

By its first issue, the Comptroller asserts that the district court erred in finding the earned-surplus amendments unconstitutional under equal-taxation and equal-protection-of-law standards because the amendments disproportionately impact fiscal-year taxpayers. We agree. The Texas Constitution requires that taxation be equal and uniform. Tex. Const. art. VIII, § 1(a). More generally, the United States Constitution requires equal protection of the laws for all persons within a state. U.S. Const. amend. XIV, § 1. However, tax legislation receives special deference. *See Vinson v. Burgess*, 773 S.W.2d 263, 266 (Tex.1989). In challenging the constitutionality of the

earned-surplus amendments, Bealls bears the burden of establishing the failure of the statute to meet constitutional requirements. *See Enron Corp. v. Spring ISD,* 922 S.W.2d 931, 934 (Tex.1996). Additionally, because no fundamental right has been affected, the Comptroller need only show that there is a rational, legitimate basis for the amendments. *See Barshop v. Medina County Underground Water Conservation Dist.,* 925 S.W.2d 618, 631 (Tex.1996).

Bealls argues that the amendments fail to meet constitutional requirements in that they have a disproportionate impact on fiscal-year taxpayers. The federal constitution does not require equality of impact among taxpayers. *See Rinaldi v. Yeager,* 384 U.S. 305, 309, 86 S.Ct. 1497, 16 L.Ed.2d 577 (1966) (holding that Equal Protection Clause does not demand statutes be applied equally to all persons). Similarly, the Texas Constitution has no such requirement. We have previously held that a tax that has a disproportionate impact is not "inherently unconstitutional so long as the legislation is rationally related to a legitimate governmental goal and the system operates equally within each class." *Beall Brothers I,* 2 S.W.3d at 567 (citing *Tandy Corp. v. Sharp,* 872 S.W.2d 814, 818 (Tex.App.-Austin 1994, writ denied)). The Comptroller argues that the tax serves legitimate governmental goals of convenience, reliability, efficiency, and conformity to federal tax periods. Furthermore, the earned-surplus amendments have a uniform starting date, reporting date, tax base, and tax rates. *See* Tex. Tax Code Ann. § 171.152(c), .1532(b), .110(a), .002(a). All taxpayers were required to pay taxes based on a twelve-month period ending on or before December 31, 1991. Therefore, all taxpayers falling within the class have been treated equally. *See Sharp v. Caterpillar, Inc.,* 932 S.W.2d 230, 240

(Tex.App.-Austin 1996, writ denied) (citing *Hurt v. Cooper,* 130 Tex. 433, 110 S.W.2d 896, 901 (1937)). Because we must give special deference to tax statutes and because the goals set forth by the Comptroller advance rational, legitimate governmental interests, we hold that there is no denial of equal taxation or equal protection in the Comptroller's application of the earned-surplus amendments to Bealls and sustain the Comptroller's first issue.

Retroactivity, Takings and Due Process Claims

By its second issue, the Comptroller contends that the earned-surplus amendments do not conflict with state or federal retroactivity, takings, or due process provisions. Article I, section 16 of the Texas Constitution provides that "[n]o . . . retroactive law . . . shall be made." Tex. Const. art. I, § 16. Retroactive application of a law is unconstitutional if it destroys or impairs a vested right. *Grocers Supply Co. v. Sharp,* 978 S.W.2d 638, 643 (Tex.App.-Austin 1998, pet. denied). Bealls bases its retroactivity claim on the fact that the taxes due for 1992 were based on income earned in 1990, before the effective date of the tax. This is because the earned-surplus computation is tied to adjusted taxable income for federal-income-tax purposes for ease of computation and efficiency. Our decision in *General Dynamics v. Sharp* controls the issue of retroactivity. *See* 919 S.W.2d 861 (Tex.App.-Austin 1996, pet. denied). In that case, the franchise tax was imposed on seven years of income, which was all reported in 1991. We held that "as long as a tax is levied after its effective date and is levied at least in part for the privilege of doing business during the current year, then it is not a retroactive tax." *Id.* at 866. Because the franchise tax in our case was levied against Bealls for the privilege

of doing business in 1992, we hold that it was not retroactively applied. Even if we construed the earned-surplus tax to apply retroactively, *General Dynamics* holds that "no Texas taxpayer has a vested right in the continuation of a particular measurement method for the franchise tax." *Id.* at 867 (citing *Smith v. Davis,* 426 S.W.2d 827, 834 (Tex.1968)).

Bealls argues that the earned-surplus amendments act as an unconstitutional taking as applied to it. Article I, section 17 of the Texas Constitution provides that "[n]o person's property shall be taken . . . for or applied to public use without adequate compensation." Tex. Const. art. I, § 17. This provision has generally been confined to eminent domain proceedings. *See Friedman v. American Sur. Co.,* 137 Tex. 149, 151 S.W.2d 570, 577 (1941). Although we recently held that takings-clause claims are not absolutely limited to eminent domain, we do not extend that holding to the facts of this case. *See Texas Workforce Comm'n v. Midfirst Bank,* 40 S.W.3d 690, 697 (Tex.App.-Austin 2001, pet. denied). *Midfirst* considered the issue of whether a state agency's withholding of funds subject to a private party's perfected security interest constituted a taking. *Id.* at 695-98; *see also County of Burleson v. General Elec. Capital Corp.,* 831 S.W.2d 54 (Tex.App.-Houston [14th Dist.] 1992, writ denied) (illegal taking occurred where taxing authority did not follow statutory procedure for foreclosure of tax lien). The State has the authority to levy and collect taxes in a rational and legitimate manner. The exercise of that authority here does not amount to a taking.

Bealls next asserts that imposition of the tax is an illegal taking under the Fifth Amendment to the United States Constitution, which provides: "private property

[shall not] be taken for public use, without just compensation." U.S. Const. amend. V. Bealls relies on *Eastern Enterprises v. Apfel*, 524 U.S. 498, 118 S.Ct. 2131, 141 L.Ed.2d 451 (1998). In *Eastern Enterprises*, the United States Supreme Court held that a provision of the Coal Act,[6] "which establishe[d] a mechanism for funding health care benefits for retirees from the coal industry and their dependents" was an unconstitutional taking, primarily because of the Coal Act's "severe retroactive liability on a limited class of parties that could not have anticipated the liability." *Id.* at 504, 529, 118 S.Ct. 2131. We do not agree that such reasoning applies to the case before us, which involves a tax, not an economic regulation. The Supreme Court was careful in limiting its decision, observing that the "extent of Eastern's retroactive liability is substantial and far reaching," and went on to note that the case was distinguishable from retroactive tax provisions that are restricted to "short and limited periods." *Id.* at 534, 118 S.Ct. 2131 (quoting *United States v. Darusmont*, 449 U.S. 292, 296-97, 101 S.Ct. 549, 66 L.Ed.2d 513 (1981)). Additionally, the tax before us is levied prospectively for the privilege of doing business in the state. Eastern was subjected to a regulation that required it to pay lifetime health benefits for employees from decades past. Unlike the tax at issue here, the regulation in *Eastern Enterprises* was not tied to any current business activity. Nor will we hold, as Bealls urges, that

> although there was a seeming exercise of the taxing power, the act complained of was so arbitrary as to constrain to the conclusion that it was not

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[6] *See* 26 U.S.C. §§ 9701-9722 (1994 & Supp. II 1996).

> the exertion of taxation, but a confiscation of property; that is, a taking of the same in violation of the 5th Amendment; or, what is equivalent thereto, was so wanting in basis for classification as to produce such a gross and patent inequality as to inevitably lead to the same conclusion.

Brushaber v. Union Pac. R.R., 240 U.S. 1, 24-25, 36 S.Ct. 236, 60 L.Ed. 493 (1916). We hold that, in enacting the earned-surplus amendments, the legislature acted within the constitutional confines of the Fifth Amendment, and Bealls may not prevail on its federal-takings-clause claim.

Bealls also raised state and federal due process claims in its motion for summary judgment. The due-course-of-law provision in article I, section 19 of the Texas Constitution contains both procedural and substantive components. Tex. Const. art. I, § 19; *Barshop*, 925 S.W.2d at 632. There has been no complaint of lack of notice and opportunity to be heard. Therefore, the requirements of procedural due process have been met. Because we hold there was no violation of equal taxation, equal protection, retroactivity, or takings provisions, we hold that the requirements of substantive due process were met. We hold that these same principles apply to Bealls' claim under the Due Process Clause of the Fourteenth Amendment to the United States Constitution. U.S. Const. amend. XIV, § 1; *see Norris v. State*, 788 S.W.2d 65, 72 (Tex.App.-Dallas 1990, pet. ref'd.) (stating that courts have historically equated due-course-of-law provision of Texas Constitution with due-process clause of United States Constitution). We hold that the implementation of the earned-surplus amendments does not offend the

constitutional principles of retroactivity, takings, or due process. We therefore sustain the Comptroller's second issue.

Business-Loss Carryovers

By its third issue, the Comptroller contends that the district court erred in allowing Bealls an apportioned business-loss carryover for report year 1992 as if it were a calendar-year taxpayer, when it is a fiscal-year taxpayer. Business losses are any negative amounts after apportionment and allocation. Tex. Tax Code Ann. § 171.110(e). They are carried forward to the year succeeding the year they accrue and are offset against that year's earned surplus. *Id.* They may be carried forward for up to four years or until they are exhausted. *Id.*

The district court apparently determined that calculating Bealls' franchise-tax liability based on earned surplus before January 1, 1991 was unconstitutional because the scheme rendered fiscal-year taxpayers subject to the tax earlier than calendar-year taxpayers would be subject to the same tax. Thus the tax should be calculated beginning at the same time for both calendar- and fiscal-year taxpayers. For calendar-year taxpayers, the initial tax period would be from January 1, 1991 to December 31, 1991. For fiscal-year taxpayers, such as Bealls, the initial tax period would be from January 1, 1991 until the end of the taxpayer's fiscal year that ended in 1992. It appears that the district court recalculated Bealls' tax based on a period from January 1, 1991 to February 2, 1991 and determined that, during such period, Bealls had an earned surplus of zero and a net operating loss. Therefore, Bealls

was entitled to carry the loss over to the following report period.

We have held that the earned-surplus amendments are constitutional. There is nothing in the tax code indicating that a business-loss carryover should be calculated for a period different from that for which the earned surplus is calculated. *See* Tex. Tax Code Ann. § 171.110. Just as the franchise tax owed by Bealls for report year 1992 was to be calculated using its February 4, 1990 to February 2, 1991 fiscal-year accounting period, *see id.* § 171.1532(b), so should the business-loss carryover be calculated using that same period. Bealls does not allege a net operating loss for such period. We hold that the district court erred in determining Bealls was entitled to a business-loss carryover for report year 1992 and sustain the Comptroller's third issue.

CONCLUSION

Having sustained all of the Comptroller's issues, we reverse the district court's judgment and render judgment that Bealls take nothing by its suit for a refund.

CAUSE NO. 96-03719

PALAIS ROYAL, INC. and 3 BEALL BROTHERS 3, INC.	§	IN THE DISTRICT COURT
v.	§	OF TRAVIS COUNTY, TEXAS
CAROLE KEETON RYLANDER, COMPTROLLER OF PUBLIC ACCOUNTS OF THE STATE OF TEXAS, AND JOHN CORNYN, ATTORNEY GENERAL OF THE STATE OF TEXAS	§	98TH JUDICIAL DISTRICT

FINAL JUDGMENT

On January 17, 2001 came on to be heard the above-entitled and numbered cause in which Palais Royal, Inc. and 3 Beall Brothers 3, Inc. are Plaintiffs ("Plaintiffs") and Carole Keeton Rylander, successor to John Sharp, Comptroller of Public Accounts of the State of Texas, and John Cornyn, successor to Dan Morales, Attorney General of the State of Texas are Defendants ("Defendants"). This Court has jurisdiction of the parties and the subject matter.

Defendants' objection to Plaintiffs' Summary Judgment Exhibit 2, Interrogatories and Responses 1-7, is overruled.

With regard to the Plantiffs' constitutional claims concerning the implementation of the earned surplus tax, the Court grants Plaintiffs' Motion for Summary

Judgment and denies Defendants' Motion for Summary Judgment.

With regard to the Plaintiffs' constitutional claims concerning officer and director compensation, the Court grants Defendants' Motion for Summary Judgment and denies Plaintiffs' Motion for Summary Judgment.

Defendants are ordered to issue one or more warrants to Plaintiff 3 Beall Brothers 3, Inc. for a refund of $373,672.18 in taxes for Report Year 1992 plus interest assessed by the Comptroller on that amount plus statutory interest provided by Section 112.060 of the Texas Tax Code. In addition, Plaintiff 3 Beall Brothers 3, Inc. is entitled to an apportioned business loss carryover of $4,345,079 for Report Year 1992.

Defendants are ordered to issue one or more warrants to Plaintiff Palais Royal, Inc. for a refund of $106,611.62 in taxes for Report Year 1992 plus interest assessed by the Comptroller on that amount plus statutory interest provided by Section 112.060 of the Texas Tax Code. In addition, Plaintiff Palais Royal, Inc. is entitled to an apportioned business loss carryover of $2,099,536 for Report Year 1992.

The Defendants will retain all other amounts paid under protest and any pro rata statutory interest accumulated on those amounts.

Each party shall bear its own costs. Relief not granted is denied.

SIGNED this 30 day of January, 2001.

/s/ Paul Davis
JUDGE PRESIDING

Approved as to form:

/s/ R. Langenberg
Counsel for Plaintiffs

/s/ Christine Monzingo
Counsel for Defendants

[LOGO] **THE SUPREME COURT OF TEXAS**
Post Office Box 12248
Austin, Texas 78711 (512) 463-1312

December 19, 2002

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Scott Douglass & McConnico
600 Congress Avenue, Suite 1500
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Ms. Christine Monzingo
Office of the Attorney General of Texas
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RE: Case Number 02-0735
Court of Appeals Number: 03-01-00224-CV
Trial Court Number: 96-03719

Style: PALAIS ROYAL, INC. AND 3 BEALL BROTHERS 3, INC.

v.

CAROLE KEETON RYLANDER, COMPTROLLER OF PUBLIC ACCOUNTS OF THE STATE OF TEXAS AND JOHN CORNYN, ATTORNEY GENERAL OF THE STATE OF TEXAS

Dear Counsel:

Today, the Supreme Court of Texas denied the motion for rehearing of the above styled petition for review.

Sincerely,

Andrew Weber, Clerk

by /s/ Jessica L. Vlasac
Jessica L. Vlasac, Deputy

cc: Ms. Diane O'Neal, Clerk
Ms. Amalia Rodriguez-Mendoza

1991 Tex. Sess. Law Serv. Ch. 5, §§ 8.02, 8.03, 8.09, and 8.14 (Vernon)

SECTION 8.02. Subchapter A, Chapter 171, Tax Code, is amended by adding Section 171.0011 to read as follows:

Sec. 171.0011. ADDITIONAL TAX. (a) An additional tax is imposed on a corporation that is subject to the tax imposed under Section 171.001 and that is no longer subject to the taxing jurisdiction of this state in relation to the tax on net taxable earned surplus.

(b) The additional tax is equal to the rate then in effect under Section 171.002(a)(2) multiplied by the corporation's net taxable earned surplus computed on the period beginning on the day after the last day for which the tax imposed on net taxable earned surplus was computed under Section 171.1532 and ending on the date the corporation is no longer subject to the taxing jurisdiction of this state in relation to the tax on net taxable earned surplus.

(c) The additional tax imposed and any report required by the comptroller are delinquent after the 60th day after the date on which the corporation is no longer subject to the taxing jurisdiction of this state in relation to the tax on net taxable earned surplus.

(d) Except as otherwise provided by this section, the provisions of this chapter apply to the tax imposed under this section.

(e) A deduction authorized under Section 171.110(a)(3) is prorated according to the length of the period on which the tax under this section is imposed.

SECTION 8.03. Subchapter A, Chapter 171, Tax Code, is amended by amending Section 171.002 and adding Section 171.0021 to read as follows:

Sec. 171.002. *RATES; COMPUTATION OF TAX* [~~GENERAL RATE OF TAX~~]. (a) The rates of the franchise tax [~~on a corporation~~] are:

(1) *0.25 percent per year of privilege period of net* [~~$5.25 for each $1,000 or fraction of $1,000 of the corporation's~~] taxable capital [~~that is allocated to this state under Section 171.106 or 171.108 of this code~~] and [~~or~~]

(2) *4.5 percent of net taxable earned surplus* [~~$68~~].

(b) The amount of franchise tax on each corporation, except as provided in Subsection (d), is computed by adding the following:

(1) the amount calculated by applying the tax rate prescribed by Subsection (a)(1) to the corporation's net taxable capital; and

(2) the difference between:

(A) the amount calculated by applying the tax rate prescribed by Subsection (a)(2) to the corporation's net taxable earned surplus; and

(B) the amount determined under Subdivision (1).

(c) In making a computation under Subsection (b), an amount computed under Subsection (b)(1) or (b)(2) that is zero or less is computed as a zero.

(d) If the amount of tax computed under Subsection (b) for a corporation is less than $100, the corporation is not required to pay that amount and is not considered to

owe any tax for that period [~~(b) A corporation shall pay the tax on the basis of the rate provided by this section that results in the greater amount of tax due from the corporation to the state~~].

SECTION 8.09. Subchapter C, Chapter 171, Tax Code, is amended by adding Sections 171.110 and 171.111 to read as follows:

Sec. 171.110. DETERMINATION OF NET TAXABLE EARNED SURPLUS. (a) The net taxable earned surplus of a corporation is computed by:

(1) determining the corporation's reportable federal taxable income, subtracting from that amount any amount included in reportable federal taxable income under Section 78 or Sections 951-964, Internal Revenue Code, and dividends received from a subsidiary, associate, or affiliated corporation that does not transact a substantial portion of its business or regularly maintain a substantial portion of its assets in the United States, and adding to that amount any compensation of officers or directors, or if a bank, any compensation of directors and executive officers, to the extent excluded in determining federal taxable income to determine the corporation's taxable earned surplus;

(2) apportioning the corporation's taxable earned surplus to this state as provided by Section 171.106(b) or (c), as applicable, to determine the corporation's apportioned taxable earned surplus; and

(3) subtracting from that amount any allowable deductions and any business loss that is carried forward to the tax reporting period and deductible under Subsection (e).

(b) A corporation is not required to add the compensation of officers or directors as required by Subsection (a)(1) if the corporation is:

(1) a corporation that has not more than 35 shareholders; or

(2) an S corporation, as that term is defined by Section 1361, Internal Revenue Code.

(c) Subsection (b) does not apply to a subsidiary corporation unless it applies to the subsidiary's parent corporation.

(d) A corporation's reportable federal taxable income is the corporation's federal taxable income after Schedule C special deductions and before net operating loss deductions as computed under the Internal Revenue Code, except that an S corporation's reportable federal taxable income is the amount of the income reportable to the Internal Revenue Service as taxable to the corporation's shareholders.

(e) For purposes of this section, a business loss is any negative amount after apportionment. The business loss shall be carried forward to the year succeeding the loss year as a deduction to net taxable earned surplus, then successively to the succeeding four taxable years after the loss year or until the loss is exhausted, whichever occurs first, but for not more than five taxable years after the loss year. Notwithstanding the preceding sentence, a business loss from a tax year that ends before January 1, 1991, may not be used to reduce net taxable earned surplus.

(f) A corporation may use either the "first in – first out" or "last in – first out" method of accounting to compute its net taxable earned surplus, but only to the extent that the corporation used that method on its most recent federal

income tax report originally due on or before the date on which the corporation's franchise tax report is originally due.

(g) For purposes of this section, an approved Employee Stock Ownership Plan controlling a minority interest and voted through a single trustee shall be considered one shareholder.

SECTION 8.14. Subchapter D, Chapter 171, Tax Code, is amended by adding Section 171.1532 to read as follows:

Sec. 171.1532. BUSINESS ON WHICH TAX ON NET TAXABLE EARNED SURPLUS IS BASED. (a) The tax covering the privilege periods included on the initial report, as required by Section 171.153, is based on the business done by the corporation during the period beginning on the day the corporation files its charter or is granted a certificate of authority or the date that a foreign corporation begins doing business in this state, whichever is earlier, and:

(1) ending on the last accounting period ending date that is at least 60 days before the original due date of the initial report; or

(2) if there is no such period ending date in Subdivision (1) of this subsection, then ending on the day that is the last day of a calendar month and that is nearest to the end of the corporation's first year of business.

(b) The tax covering the regular annual period, other than a regular annual period included on the initial report, is based on the business done by the corporation during the period beginning with the day after the date upon which the initial report is based, as required by Subsection (a) of this section, and ending with its last accounting period

ending in the year before the year in which the report is originally due.